



City Council Housing Subcommittee

Affordable Housing and Economic Considerations – CSCDA Community Improvement Authority Proposal for the Turing Apartments

September 2, 2021

City of Milpitas

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Background

- May 11, 2021: City Council meeting
 - Councilmember Phan: Discuss and provide direction to staff on an opportunity to create middle-income workforce housing through the California Statewide Communities Development Authority (CSCDA)
 - Council direction:

Staff to enter into agreement with consultant to conduct a study (not at City expense; to be paid for by project owner) to explore the CSCDA proposal for a specific site within the Fields Project.

Information to be distributed to Council at a future meeting.



Affordable Housing and Economic Considerations CSCDA Proposal for Turing Apartments

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KEYSER MARSTON ASSOCIATES, INC.

September 2, 2021

PURPOSE OF KMA REVIEW

- Affordable housing benefits
- Financial returns to the City relative to the cost of foregoing property tax revenue for 30+ year term
- The structure of the transaction and potential risks to the City
- Survey other cities that declined to participate in similar offer by CSCDA

CSCDA PROGRAM

- Recently formed joint powers authority
- Mission is production of Moderate –Income Housing
- At least 12 projects have closed financing
- Waterford has been the most active group in California in 2021 with \$1.2 billion in bond issuances.
- Waterford project locations: Pasadena, Glendale, Long Beach, and Anaheim (2 projects)

PROGRAM STRUCTURE

- The Authority will issue tax exempt bonds to acquire the Project and fund reserve accounts, capital replacement reserves, and provide up-front payments to the Administrator, and CSCDA
- Repayment of the bonds is secured solely by the revenues generated by the Project. The City bears no responsibility for the operation of the Project or the repayment of the bonds

PROGRAM STRUCTURE CONTINUED

- The bond term is 30+ years
- The City can call for a sale after year 15 if proceeds are sufficient to retire outstanding debt
- The Project would be conveyed on an “as is” basis and the City or future owner would be responsible for making repairs
- The City would receive all available net sales proceeds

CREATING AFFORDABILITY

- Once acquired by the Authority, the Project will be exempt from paying ad valorem property taxes
- The savings created by the abatement of property taxes is used to reduce the Project's rents and restrict rents to Moderate income levels throughout the bond term

TURING APARTMENTS



TURING APARTMENTS – UNIT MIX AND CURRENT RENTAL RATES

Unit Type	Units	% of Units	Avg. SF	Effective Rent	Rent per SF
Studios	19	5%	563	\$2,278	\$4.05
1 Beds	193	52%	778	\$2,923	\$3.76
2 Beds	150	40%	1,157	\$3,427	\$2.96
3 Beds	9	2%	1,667	\$5,327	\$3.20
Total	371	100%	942	\$3,155	\$3.35

AFFORDABILITY CONSIDERATIONS

CURRENT MARKET RENTS AT TURING COMPARED TO OTHER MARKET RATE UNITS IN MILPITAS

Unit Type	Current Monthly Average Rental Rate		
	<i>Turing</i>	<i>Market Rate Units in Milpitas</i>	<i>Difference</i>
Studio Units	\$2,278	\$2,155	\$123 (+6%)
One Bedroom Units	\$2,923	\$2,376	\$547 (+23%)
Two Bedroom Units	\$3,427	\$2,887	\$540 (+19%)
Three Bedroom Units	\$5,327	\$3,317	\$2,010 (+61%)
Avg, all Units	\$3,152	\$2,595	\$560 (+22%)

PROPOSED AFFORDABLE PROGRAM

Units to be affordable to tenants earning 80% to 120% AMI, per CSCDA maximum income and rent formulas

- 33% of units at 80% AMI
- 33% of units at 100% AMI
- 33% of units at 120% AMI

Administrator anticipates a 3-year transition period for all units to convert to income eligible households

PROPOSED RENTAL RATES

Existing Income-eligible tenants

- 80% AMI units: 12% reduction; or \$400 per month
- 100% AMI units: 10% reduction; or \$315 per month
- 120% AMI units: 8% reduction; or \$253 per month
- Average 10% Reduction; or \$322 per month

New income-eligible tenants

- Rent cannot exceed CSCDA limits

Maximum annual rent escalation on existing tenants: % growth in AMI or 4%, whichever is less

PROPOSED RESTRICTED RENTS FOR EXISTING INCOME-ELIGIBLE TENANTS

	Studios	One Bedrooms	Two Bedrooms	Three Bedrooms	Average
Current Turing Rents	\$2,278	\$2,923	\$3,427	\$5,327	\$3,155
Proposed Reduced Rents for Existing Income-Eligible Tenants					
80% of AMI	\$2,004	\$2,572	\$3,015	\$3,866	\$2,755
100% of AMI	\$2,050	\$2,631	\$3,084	\$4,794	\$2,839
120% of AMI	\$2,096	\$2,689	\$3,152	\$4,900	\$2,902
Average	\$2,050	\$2,631	\$3,084	\$4,520	\$2,832
Proposed Rent Reduction					
80% of AMI	(\$274)	(\$351)	(\$412)	(\$1,461)	(\$400)
100% of AMI	(\$228)	(\$292)	(\$343)	(\$533)	(\$315)
120% of AMI	(\$182)	(\$234)	(\$275)	(\$426)	(\$253)
Avg. Rent Reduction	\$228	\$292	\$343	\$807	\$322
Percent Reduction	11%	9%	10%	15%	10%

MAXIMUM RENTS ON UNITS ON VACATED UNITS

Standard CSCDA Limits: rent set at 35% of income + utilities

	Studios	One Bedroom	Two Bedroom	Three Bedroom	Avg.
80% AMI	\$2,707	\$3,094	\$3,481	\$3,866	\$3,251
100% AMI	\$3,383	\$3,868	\$4,352	\$4,833	\$4,064
120% AMI	\$4,060	\$4,641	\$5,222	\$5,800	\$4,876
Average	\$3,383	\$3,868	\$4,352	\$4,833	\$4,064

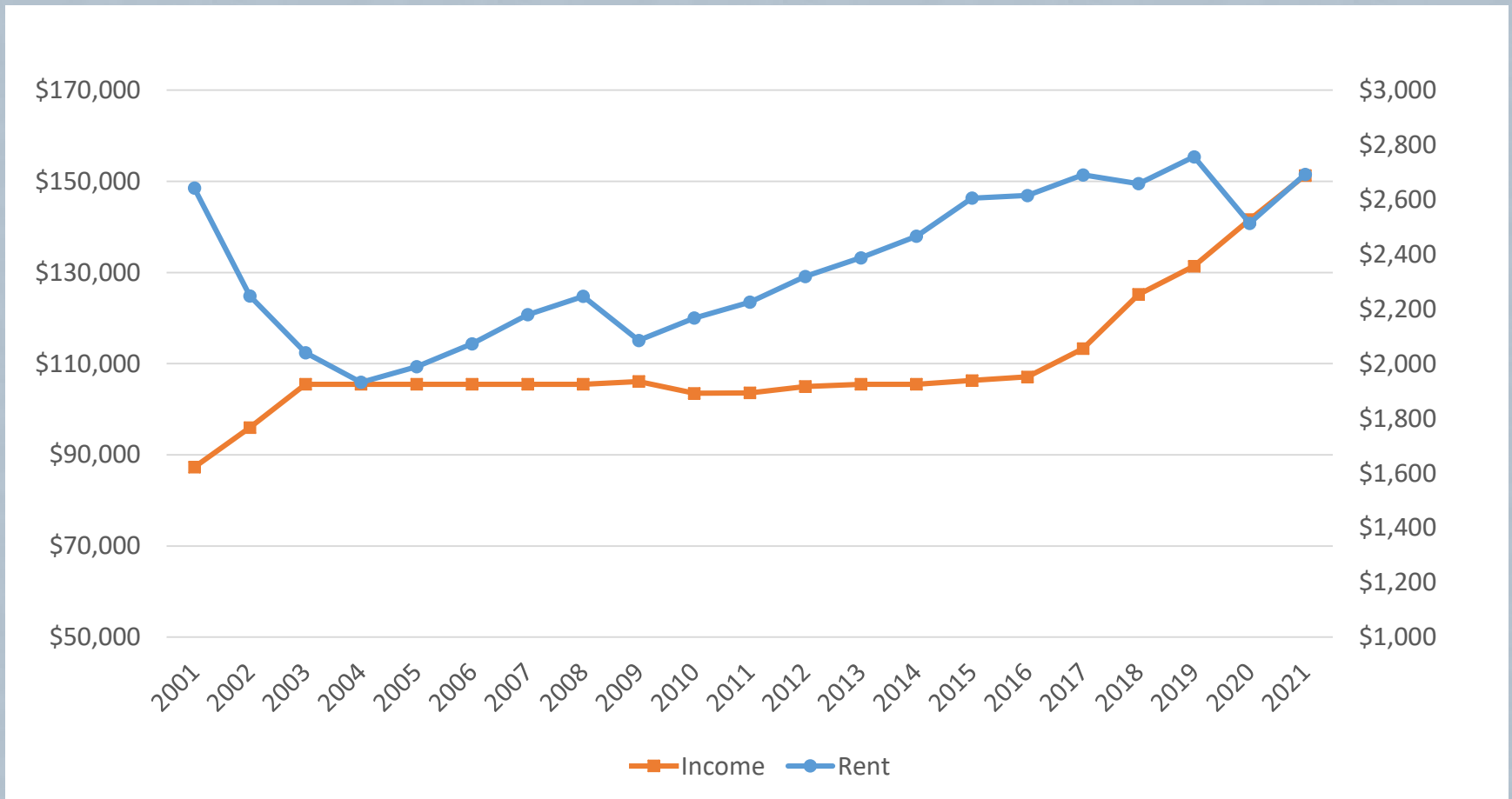
MAXIMUM RENTS UNDER CSCDA LIMITS COMPARED TO MAXIMUM RENTS UNDER HCD REGULATIONS

	Studios	One Bedrooms	Two Bedrooms	Three Bedrooms	Average
Maximum CSCDA Rents					
<i>Average</i>	\$3,383	\$3,868	\$4,352	\$4,833	\$4,064
Maximum HCD Rents					
<i>Average</i>	\$2,451	\$2,818	\$3,163	\$3,509	\$2,957
Difference					
<i>Average</i>	+\$932	+\$1,050	+\$1,188	+\$1,324	\$1,107
					37%

COMPARISON OF RENTS

	Weighted Average, weighted by Turing Unit Mix	Difference between Rent and Newer Mkt. Area Rate	Percent Difference
CSCDA Maximum for New Tenants	\$4,064	\$1,324	48%
Current Turing	\$3,155	\$415	15%
HCD Maximum	\$2,957	\$217	8%
Proposed Rents for Existing Income Eligible Tenants	\$2,830	\$90	3%
Citywide Mkt. Rate Rent, Units Built since 2014	\$2,740	\$0	0%
Citywide Mkt. Rate, all Units	\$2,595	-\$145	-5%

AREA MEDIAN INCOME AND MARKET RENTS



GROWTH IN AREA MEDIAN INCOME COMPARED TO MARKET RENTS IN MILPITAS, 2001- 2021

Year	Area Median Income		Milpitas Market Rate Apts.	
	4-person Household	% Change	Market Rate Apartment Rents	% Change
2001	\$87,300		\$2,642	
2002	\$96,000	10%	\$2,247	-15%
2003	\$105,500	10%	\$2,040	-9%
2004	\$105,500	0%	\$1,932	-5%
2005	\$105,500	0%	\$1,989	3%
2006	\$105,500	0%	\$2,073	4%
2007	\$105,500	0%	\$2,179	5%
2008	\$105,500	0%	\$2,246	3%
2009	\$106,100	1%	\$2,085	-7%
2010	\$103,500	-2%	\$2,167	4%
2011	\$103,600	0%	\$2,225	3%
2012	\$105,000	1%	\$2,319	4%
2013	\$105,500	0%	\$2,387	3%
2014	\$105,500	0%	\$2,466	3%
2015	\$106,300	1%	\$2,605	6%
2016	\$107,100	1%	\$2,615	0%
2017	\$113,300	6%	\$2,690	3%
2018	\$125,200	11%	\$2,658	-1%
2019	\$131,400	5%	\$2,756	4%
2020	\$141,600	8%	\$2,513	-9%
2021	\$151,300	7%	\$2,692	7%
Average Annual Change, 2001-2021:		2.9%		0.3%
Average Annual Change, 2009-2019:		2.2%		2.8%

AFFORDABILITY CONCLUSIONS

- The program would provide 371 deed-restricted Moderate-income units for approximately 30 years.
- Rental rates paid by existing income eligible tenants would decrease, on average, 10%, or \$323 per month to an average rate of \$2,832 per month.
- The average proposed reduced rental rate exceeds the average citywide rental rate for market rate apartments.
- Given that the rents on new leases would be governed by the CSCDA limits and those limits permit rents that exceed current market rate Turing rents and the cash flow pro forma relies on an average annual growth rate of 3%, it is likely that the rents paid by new tenants will exceed the rents paid by existing tenants and may approach market rates.
- The rent restrictions will not provide with the City with any RHNA credit.
- Given these considerations, the near-term affordability benefits are very limited.
- Future affordability benefits will hinge on market rate rents increasing at a faster rate than 3% per year.

FINANCIAL CONSIDERATIONS

CITY INVESTMENT AND RETURNS

- The City's investment would be limited to foregoing ad valorem property taxes and payments from the state in the form of property tax revenue in-lieu of motor vehicle license fees over the bond term
- If City elected to sell the property, City would receive all net sale proceeds after retiring all outstanding debt
- City could elect for the property to remain as affordable housing

ESTIMATED FOREGONE PROPERTY TAX REVENUES TO TAXING AGENCIES, FY 2021-22

Assessed Value		
Land & Improvements		\$186,491,455
Personal Property		<u>\$1,599,901</u>
Project Assessed Value		\$188,091,356
General Levy (1% of Assessed Value)		
City of Milpitas	16.24%	\$305,460
Milpitas Unified	40.08%	\$753,870
San Jose Evergreen Community College	6.50%	\$122,259
County School Service	3.16%	\$59,437
ERAF	14.78%	\$277,999
Santa Clara County	14.03%	\$263,892
Bay Area Air Quality Management District	0.18%	\$3,386
Santa Clara County Importation Water - Misc District	0.49%	\$9,216
Santa Clara County Library	2.56%	\$48,151
Santa Clara Valley Water District	0.16%	\$3,009
Santa Clara County Water District Zone 1	1.69%	\$31,787
Santa Clara County Water District Zone 4	0.13%	\$2,445
Total General Levy	100.00%	\$1,880,914

ESTIMATED FOREGONE PROPERTY TAX REVENUES TO TAXING AGENCIES, FY 2021-22, CONT'D

Assessed Value		
Land & Improvements		\$186,491,455
Personal Property		<u>\$1,599,901</u>
Project Assessed Value		\$188,091,356
Voted Indebtedness		
County Retirement Levy	0.0388%	\$72,979
County Library Retirement	0.0024%	\$4,514
Elementary or Unified School Bonds	0.0898%	\$168,906
Community College Bonds	0.0357%	\$67,149
<u>County Bond 2008 Hosp Fac</u>	<u>0.0069%</u>	<u>\$12,978</u>
Subtotal	0.1736%	\$326,527
SCVWD-State Water Project (Land & Imp Only)	0.0037%	\$6,900
Total Voted Indebtedness		\$333,427
Property Tax In-lieu of Motor Vehicle License Fees (PTILVLF)		\$75,237
Total Foregone Property Taxes to Taxing Agencies, FY2021-22		\$2,289,577

PROJECTED ABATED PROPERTY TAXES AND FOREGONE MILPITAS PTILVLF REVENUE DURING REGULATORY PERIOD

	Year 1	Year 15	Year 30
All Taxing Entities			
Annual (Increases @ 2% per yr)	\$2,289,577	\$3,021,048	\$4,065,933
Cumulative (Discounted @ 3%)		\$31,170,000	\$58,096,000
City of Milpitas			
Annual (Increases @ 2% per yr)	\$380,697	\$502,321	\$676,059
Cumulative (Discounted @ 3%)		\$5,183,000	\$9,660,000

Source: Turing FY2020-21 Secured Property Tax Bill, Santa Clara County Assessor data.

FUNDING FOR CAPITAL IMPROVEMENTS

- Bond proceeds will fund a \$3.1 million capital account
- Property Condition Report indicates that \$3.1 million will be sufficient to fund capital needs for 12 years
- Annual cash flow will provide additional funding
- Total funding of \$7.6 million in 2021 dollars is anticipated over 34 years.
- This level of funding is likely insufficient to fund needed improvements throughout the bond term
- A portion of sale proceeds would need to be used to fund improvements to ready the property for sale

PROJECTED FINANCIAL RETURNS TO CITY OF MILPITAS

Sale in Year 30, \$millions	Scenario A: Waterford Projection (3% Annual Growth in Rental Income)	Scenario B: Less Aggressive Projection (2% Annual Growth in Rental Income +\$28.2 million capital improvement in year 30)
Net Proceeds After Debt	\$324.7	\$102.4
Foregone City Property Taxes and Property Taxes In-lieu of Motor Vehicle License Fees	\$15.4	\$15.4
Net Return to City After Reimbursement of Foregone City Taxes and \$28.2 million additional capital improvement (Scenario B)	\$309.2	\$58.8
Net City Return in 2021 Dollars if only Foregone City Taxes are Reimbursed and \$28.2 million of additional capital improvements are funded (Scenario B)	\$127.4	\$24.2
Net City Return in 2021 Dollars if All Taxing Agencies Are Reimbursed	\$95.5	\$0 (Net Proceeds are insufficient to provide full reimbursement to taxing agencies)

THE FINANCING

- The Project's financing does not require any cash equity and the repayment of debt is secured by the Project's cash flow.
- The bonds are not likely that the bonds will receive an investment grade rating.
- Structure provides significant up-front compensation to the Administrator, CSCDA, and the current owner.
- In contrast, the returns to the bond holders and the city are entirely at risk and subject to the performance of the Project

PROPOSED PAYMENTS

	Funded from bond proceeds	Funded from cash flow
Seller of Turing (affiliate of Lyon Living)	\$235,250,000	None
CSCDA	\$1,250,000	Year 6+: \$250,000 annually
Administrator (Waterford)	\$4,250,000 up front; \$5,000,000 upon sale after year 15	Year 6+: \$250,000 annually, escalated at 3%
Greystone	None	1.75% of gross effective income; \$18,000 monthly minimum.
Costs of Issuance	\$7,421,000	

FINANCIAL CONCLUSIONS

1. Over a 30-year period, it is estimated that the City would forego a total of \$15.4 million (\$9.7 million in 2021 dollars) of ad valorem property tax revenue and property taxes in lieu of vehicle license fee revenue.
2. The projected performance of the Project is dependent on numerous factors. Small deviations from projected rent increases, interest income, and operating expenses could have significant impacts on the Project's ability to pay down the outstanding bond principal, viability, and yield sales revenue to reimburse the City for foregone property tax revenue.
3. The Project's funding for capital reserves appears to be inadequate to meet the Project's needs throughout the 35-year projected regulatory period.

FINANCIAL FEASIBILITY CONSIDERATIONS CONT'D

4. The sale of the Project at the end of the 30-year term could potentially yield significant proceeds to the City. As projected by Waterford, the City could receive a net return of \$95 million (2021 dollars) if the Project is sold at fair market value, no capital improvements are needed and all taxing agencies are reimbursed.
5. If the projection is modified to reflect a more conservative assumption regarding rent increases (2% per year rather than 3%) and includes a capital investment in year 30, the projected return to the City drops dramatically. Under that scenario, it is projected that net sales revenues would not be sufficient to reimburse all taxing agencies for foregone property tax revenues and fund the capital replacement investment. If the City only reimburses itself and funds the capital investment, it is anticipated that the City's net return would approximate \$24.2 million in 2021 dollars. This return is marginal given the level of risk involved with the Project.
6. The Project's financing does not require an investment of cash equity and all debt is secured solely by the revenue generated by the Project. The structure provides significant up-front compensation to the Administrator, CSCDA, and the current owner of the Project. In contrast, potential financial returns to the bond holders, the City and other taxing agencies are subject to the financial performance of the project.

PRELIMINARY RECOMMENDATIONS

RECOMMENDATIONS

If the City elects to participate in the CSCDA program, we recommend the following:

1. The rent reductions should be set at levels that are below market rate levels in Milpitas so that the Project truly delivers enhanced affordability.
2. Rent and income restrictions contained in the Regulatory Agreement should conform to the Department of Housing and Community Development (HCD) income and rent formulas.
3. The Property Condition Report should address the Project's needs for a 34-year term and the Project's financing plan provide funding to cover the anticipated capital improvement costs over the 34-year term. Any refinancing of Project debt should be subject to the City's approval.
4. The Project should be required to submit proposed rent increases to the City's approval to ensure that the affordability restrictions are enforced.
6. The Project's cash flow projection should be based on more conservative assumptions to reduce the level of risk and provide greater assurance for long-term viability.
7. The bond underwriting assumptions should be reviewed by an underwriter retained by the City and the City's Financial Advisor to ensure that the financial structure is sound and consistent with industry standards for multifamily revenue bonds and is appropriate for the City's participation.

RECOMMENDATIONS (CONT'D)

8. The Project should be required to submit an annual report to the City demonstrating that the affordability covenants are being properly implemented and enforced.
9. The Administrator should be obligated to certify that the affordability covenants are being properly implemented and enforced.
10. Greystar should be required to submit its tenant selection plan, maintenance plan, staffing plan and marketing plan for the City's approval.
11. Greystar should be required to submit annual reports on the Project's operations, including the Project's rent roll, that clearly track the annual increase in rental rates, operating expenses, capital improvements, vacancy rates, bond interest and redemption payments, and all bond specific payments.

Next Steps

- September 2, 2021: City Council Housing Subcommittee meeting
- September 21, 2021 (tentative): City Council meeting
 - Informational discussion
- October 19, 2021 (tentative): City Council meeting
 - Consideration and action



A photograph of the City of Milpitas building at dusk. The building is a modern, curved structure with a large glass facade on the right side, reflecting the interior lights. The foreground features a fountain with several water jets. A semi-transparent white box with a thin border is centered over the image, containing the city's name and contact information.

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